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IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 8.2.2006

CORAM

THE HONOURABLE MR.JUSTICE P.D.DINAKARAN
AND
THE HONOURABLE MR.JUSTICE P.P.S.JANARTHANA RAJA

TAX CASE No. 52 of 2000

The Commissioner of Income Tax
Madurai ..Applicant

Vs.

Sri M.Kathiresan ..Respondent

Reference under Section 27(1) of the Wealth Tax Act, 1957 by the Income Tax Appellate Tribunal, `A' Bench, Chennai in R.A. No. 160/Mds/96 in I.T.A. No.1770/Mds/89 for the assessment year 1983-84 against C.No.401/1/69/87-88 order dt. 23.3.89 for the assessment year 1983-84 on the file of the Office of the Commissioner of Income Tax, Madurai and PAN-47-029-PT3471/II(2)Mdu Order dt. 16.1.87 for the assessment year 83-84 on the file of the Income Tax Officer, Circle II (2) Madurai.

For Applicant :: Mrs. Pushya Sitaraman,
Senior Standing Counsel
For Respondent :: No appearance

J U D G M E N T

(Judgment of the Court was delivered by
P.D.DINAKARAN,J.)

At the instance of the Revenue, the Income-tax Appellate Tribunal has stated a case and referred the following question of law for our consideration:

> "Whether on the facts and in the circumstances of the case, the Tribunal is correct in law in holding that in the case of conversion of proprietary business into partnership firm, the stock should not be valued at market price?".

2. The assessment year involved is 1983-84. The issue

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raised in this tax case reference is regarding the method of valuation to be adopted. In the assessment proceedings for the assessment year 1983-84 the assessee claimed loss incurred in the sole proprietary concern, since the proprietary concern was converted into a partnership firm. The Income-tax Officer, completed the assessment accepting the loss returned by the assessee in the sole proprietary concern. The Revenue carried the matter in appeal before the Commissioner of Income Tax (Appeals) and the Commissioner of Income-Tax (Appeals) set aside the assessment order on the ground that the assessing officer has not revalued the stock according to market price on the conversion of the proprietary business into a partnership business, following the decisions in the case of G.R.Ramachari & Bros VS. (41 ITR 142) and A.L.A. Firm v. Commissioner of Income Tax (102 ITR 622) and directed the assessing officer to apply the ratio laid down in the above cases. On appeal by the assessee, the Income-tax Appellate Tribunal set aside the order of the Commissioner of Income Tax (Appeals), following the Supreme Court decision in the case of SUNIL SIDDARTHBHAI V. COMMISSIONER OF INCOME TAX (156 ITR 509), on the ground that though the conversion of a proprietary business into partnership is undoubtedly a transfer, it could not be said that the nominal value credited to capital account in the hands of the firm is the consideration for the transfer. It is against the order of the Income-tax Appellate Tribunal, at the instance of the Revenue, the Income-tax Appellate Tribunal has stated a case and referred the question of law referred to above.

3. Heard Mrs.Pushya Sitaraman, learned Senior Standing counsel for the Revenue, who fairly concedes that the issue raised in the above question of law is covered against the Revenue by the decision of the Supreme Court in SAKTHI TRADING CO. VS. COMMISSIONER OF INCOME TAX (250 ITR 871) and the decision of this Court in K.SHANMUGANATHAN VS. COMMISSIONER OF GIFT-TAX (264 ITR 431).

4. It is an established rule of commercial practice and accountancy that where there was no discontinuance of business, the closing stock is to be valued at cost or market price, whichever is lower by conversion. The Supreme Court and this Court in the decisions cited supra, held that since there was no cessation of business, the closing stock had to be valued at cost or market price, whichever was lower.

5. We find that the Appellate Tribunal has rightly held that though the conversion of a proprietary business into partnership is undoubtedly a transfer, it could not be said that the nominal value credited to capital account in the hands of the firm is the consideration for the transfer. It is only when the business is closed for ever, the question of valuing the stock at the market price might arise. In this case, it cannot be said that the

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assessee has ceased to remain in the same business, when he converted his proprietary business into a partnership. That apart the Revenue has also not placed any material before the Appellate Tribunal to sustain its claim that the stock should be valued at market price. In the absence of any material placed before the Appellate Tribunal, we hold that the Appellate Tribunal was justified in coming to the conclusion that the closing stock should not be valued at market price. Accordingly, we answer the question of law referred to us in the affirmative, against the Revenue and in favour of the assessee.

Sd/
Asst.Registrar

/true copy/

Sub Asst.Registrar

Msk

To

1. The Assistant Registrar,
   Income-tax Appellate Tribunal,
   Rajaji Bhavan, Besant Nagar,
   Chennai 600 090

2. The Commissioner of Income-tax (Appeals),
   Madurai.

3. The Income-tax Officer, Circle II(2), Madurai.

+1cc to M/s. Pushyasitaraman, Senior Standing Counsel SR 5771
+1cc to Philip George, Advocate Sr 6564

JE (CO)
km/4.4.

Tax Case No.52 of 2000

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